

Chairman Snow

This is the pending Southern Wine & Spirits applications, W 22-2514 and W 22-25148. They're different numbers? 149 and 148. What did I say? Old age is a dangerous thing. That's what I have here. Now this is a long-standing petition and application. It is no secret that there's been a ton of work done on this. I came into the commission, it seems like three years ago, March 23<sup>rd</sup>, and one of the first files I had on my desk was this file. It was a good size file then. It hasn't grown smaller during my stay. I'm opening with that because the file has had our attention. It has been handled by excellent, legal counsel. I assure you I have reviewed every word in the file many times, and my fellow commissioners, I'm sure, have done the same. Having opening with that because there's going to be a time here momentarily where we are not requiring public comment and statements. It's not required. We're certainly not going to stop you. If there is going to be further public comment and statements, we're just going to have to strictly enforce reasonable time limits. This is a discretionary body. It's one of my favorite words, actually. I could say that all day. Twenty minutes against; twenty minutes for, at a maximum. On the twenty minutes, the Chair will not count a preliminary motion. I know counsel...are you Rebecca?

Ms. Howard

Yes.

Chairman

Nice meeting you, having never made your acquaintance. You have a pending motion to strike something?

Howard	Motion to Disregard. Yes.
Chairman	Talk to me about that.
Howard	We currently have a Motion to Disregard on the table based on the fact that National was previously denied the opportunity to be a party and to intervene, and; therefore, we do not feel their findings of fact should be...we believe they should be disregarded by the Commission.
Chairman	The other side of that?
Steve Badger	Your Honor, I'd be happy to address that, briefly. The rules of this commission distinguish between the intervener/remonstrator and a remonstrator. We filed a motion to seek intervener status, which was denied. That does not preclude public comment as a remonstrator under this body of rules and in our views it's another way...I would remind the Commission that one of the major issues of this application, these applications is a joint venture, which the applicant never disclosed to the Commission, involves a relationship with a current permittee and we brought that to your attention. I think our participation here will add to the Commission's consideration.
Chairman	What my take on this is this. I come from a background where we get a lot of proposed findings of fact and conclusions of law. In my earlier life, twenty years on the bench, I never signed off on one of those in twenty years, because they normally are...they come in at you with a slant. And, that's okay. That's part of the process. So, I

viewed that when I got it...I think your motion is well taken. It's part of the public record. I can't start erasing things in my record. Rather than disregard it entirely, my reading of it, and I think my commission members share my opinion, it takes the form of further argument. That's how I took it. It's not going to be signed, but I can't throw it away. Is that okay? Does that work?

Howard Yes. Thank you.

Chairman That's how we'll do it. We got that out of the way. I know twenty minutes doesn't seem like that much time to you good people. I know how important this is to everybody. It's gotten a fair amount of attention. But, all I can say is we have really looked at this. I cannot over-emphasize the time that we've taken with this. So, to the extent that we're going to get into comment, you may each assume that we are well aware of the record as it exists, the public record. Having said that, I said...what did I say? Against, I'll let against go first. Any comments against?

Paul Mannweiler Paul Mannweiler, Bose McKinney & Evans.

Chairman Let's go ahead and transcribe. Not transcribe, but record.

Mannweiler In light of your comments, I'll take 30 seconds. Mr. Chairman, members of the Commission, I just want to thank you for your patience and your consideration. Obviously, with the attention and the effort you put into this and your hardworking staff has put into this, you believe this is an important matter. We think this decision will shake the

Indiana wholesale market into the 21<sup>st</sup> Century, so we feel it is very important. With that, Mr. LaCrosse is here. He has been the president and CEO of National Wine & Spirits. He has more than 35 years experience in the Indiana alcoholic beverage market. Has not only owned the operation in Indiana, but at one point in Illinois, Michigan and Kentucky and was president in 1993 of the Wine & Spirits Wholesalers of America, his national experience and exposure. With that, let me turn it over to to...Steve, do you want to start?

Badger Yes.

Chairman I will note that I read through the transcript of another public hearing that was held before I got here and I don't think Mr. LaCrosse participated in that. I just wanted to...

Jim LaCrosse Can we bring another chair over?

Chairman Absolutely. I want you to be as comfortable as you know how to be.

LaCrosse Well, I'm old.

Chairman You're in good company.

Badger Appreciate the opportunity. I will delve into not repeating our earlier comments and written submissions. On the board is sort of a roadmap of the points and reasons we believe the applications should be denied. But, I do appreciate the opportunity to address these points again, particularly in light of the Excise report that has been submitted. The main thing, lay aside what happens to

National. We're not arguing that. The real issue in front of the Commission is what's going to happen. There's real harm to the consumer if these applications are granted. The Indiana market will be dominated by Southern Wine & Spirits and its joint venture partner, Glazer/Olinger. The Excise report confirms that Glazer is 50% owner in Olinger. Southern doesn't have a license today, yet, the impact of the joint venture has already been felt. We've seen brands move, been moved from National to Olinger. Patron situation we mentioned. Originally, they said they said that, told us that we're moving to Southern and then when they were advised that Southern doesn't have an application in Indiana, "Oh, must be Glazer." This is part of a transfer that's happened in other states, as well, where the Patron brand has been moved. That's collaboration there between ostensible competitors. They are working together, divide up suppliers, and shifting suppliers one to another. That's something you need to be very concerned about. As the old saying goes, "Actions speak louder than words", and, those actions are pretty loud, speak loudly, indeed, I believe. We have not heard very much in this body from the petitioner concerning the joint venture. I have a couple of exhibits.

Chairman Kim, do you have one of these?

Kim Chew No.

Chairman You should. Do you have one for Kim?

Badger

What you have is a press release that was released just over a year ago in which a few key points there is they announced a formation of a new joint venture with a new name and a new entity, Southern/Glazer's Distributors of America. They named a management team that the Excise report points out, which are named here in the exhibit. It mentions three goals for simplification for suppliers: lower costs; increasing account penetration, that is market share gain, a national foot print focus; and national marketing strategies. They say the key is local execution, i.e., coordination and collusion in each state, which we've already seen here in Indiana. A few months later, Mr. Harvey Chaplin, who is the chief executive officer of Southern...the guy in charge anyway, provided an interview to IMPACT, a trade publication, which, "Is it a merger? It's not a merger. Then what is it? ...we're just going to pool our businesses with purchasing and buying area that affects internal supplying...not suppliers." That's what we've seen and practice that it is with suppliers. We've seen that by their actions and that's not what they said in their press release. It's just an internal thing where we need to save money on infrastructure, basically. Then, it says, when he is pressed, "I'm not at liberty to discuss anything more specific about that." In everything that has been written, we've had lots of papers submitted on behalf of Southern, but the amount of material devoted to explaining the joint

venture is virtually nonexistent. The Excise report points out, and I think about as kindly as they can say it, that they've been very, vague about the joint venture. That is about as kindly as you can say it. When the Excise officers asked for clarification, the response they got was very, carefully worded. No definitive agreement has yet been signed. That leaves—that answers very little and leaves the basic question still unanswered despite all the effort that's been put forth here to get to the bottom of it. At this point, let me turn to Mr. LaCrosse to explain how competition amongst supplier—between wholesaler for supplier relationships is important and also to discuss some of the press releases, statements in the press release. How do wholesalers compete with one another in a healthy market?

LaCrosse I guess I have to stand up.

Badger You don't have to. I do. It's old habit.

Chairman Well, it's an old habit and I'm a believer in people—people are nervous enough in these situations. Don't put any pressure on yourself. You be comfortable and the other side the same way.

LaCrosse I would think by now I wouldn't be nervous, but...when I got into business there were 22 wholesalers here in Indiana. We were all dual and triple on everything. Suppliers were really not an issue. As the business consolidated at the supplier level, we also consolidated at the distributor level until 1987, Indiana came down to basically two

wholesalers—ourselves and Olinger. In the meantime, the suppliers consolidated down to where there are five major suppliers that control probably 75% of the spirits' business. We are, and most wholesalers are, basically spirits suppliers. Even though 50% of our cases are wine, 80% of our revenue is still spirits. Without spirits we couldn't exist. There are a huge number of wine suppliers, but in the spirits' business there are only five and we all really depend on keeping our business alive. That basically comes down to one wholesaler has two major suppliers and the other wholesaler has three major suppliers. Southern—and that's really where the competition is. It's for suppliers. Somebody asked me one time, "how do you get retailers?" and I said if you get absolute, the retailers have to buy from us, whether they like us, whether we give good service, whether we do anything for them. Obviously, we try to do all of those things well. But, the competition is at the supplier level. Somewhere I saw one of Harvey's interviews that they do 50% of Jim Beam's business. Jim Beam is our second largest supplier. They do—they are the national wholesaler for the Pernod Company. Pernod is our third largest supplier. They're a huge Diageo distributor and Diageo is our first largest supplier. What they've done is basically eliminated competition from suppliers. I would describe it as a monopoly, although I understand that you have to go to court and have some legal definition of what monopoly is,

but in our view Southern is really the 800 lb gorilla. We have been told when Southern applied for an application by two of our supplier that we should start talking to Southern and start talking to somebody else to partner, which we have done. But, their mere application to the State started our suppliers telling us that we either have to partner with somebody, or sell out to Southern.

Badger                      Would you comment on national programs and pricing that was mentioned in the...

LaCrosse                    Yes. They have a national sales force. They called on National chain accounts. We do not. All of our suppliers have national sales forces that call on the chain stores and (inaudible) programs and pricing. The problem we have, especially with this joint venture where National and Glazer will be calling on national chain stores, is in the area of pricing. When you call on an account, the number one thing they are interested in is price. It's bad enough when a company like Southern calls on a national chain program and sets prices. It's even worse now when National and Glazer call on and set prices where basically all the products in the market and that comes down to a serious violation of the Indiana pricing laws where we are required to offer the same price to everybody in the market. They're making national chain calls and setting prices that give the national chains an edge. They are denying the local package stores and the local stores the same price.

Badger But, what's the impact of Southern's entry if the license is granted?

LaCrosse The impact on local stores will be severe. The regional impact, if we want to talk about regional pricing—Indiana happens to sit in between Illinois and Ohio. I don't think we can change that and Kentucky on the south and Michigan on the north. They have operations in Illinois, Ohio and Kentucky. We actually compete on a price basis with Illinois and Kentucky. For them to ---and right now our prices are 2-3 dollars lower than Illinois, because they just took an 18 – 24 dollar a case increase in Illinois and our prices are lower. We're going to get a substantial amount of business out of Illinois. Were Southern to get a license in this region, they will focus on regional pricing, which would mean a substantial increase in the Indiana pricing. They would not want to sell cases at a lower profit in Indiana than what they sell for in Illinois.

Badger Can you clarify one thing that you said? I think you may have misspoke. You said National and Glazer will be calling on national accounts. Do you mean Southern and Glazer?

LaCrosse Yes. Southern and Glazer have said they are going to combine their national sales organization.

Badger There's no dispute here that granting the permits would place an unprecedented level of control in the Indiana market in the hands of this unified management team that

they announced, Southern and Glazer's joint venture. That is simply not a situation that would be good for the Indiana consumer. I've given you a handout on the language and the statute and the reason for that is the 1962 Attorney General's Opinion sets forth this Commission's power and authority to review anticompetitive practices. That's just as alive today under the current – if anything, the statute is stronger than it was at that time in 1962. This is not a problem, Southern's entry here, that the Commission should kick down the road. As we've indicated, once Southern's presence is established here, they are going to quickly become the dominant player and with the joint venture with Olinger and Glazer, have the ability to control the market. Let me turn now to, just very briefly, I know I'm probably running short on time.

Chairman

Just a little under five minutes remain.

Badger

Okay, thank you, Your Honor. I appreciate that. The lack of candor that has been shown and I'll just touch briefly on these points. I think they are pretty well laid out in the Excise report, or at least mentioned there. The most serious failure of disclosure is, of course, the failure to disclose the joint venture itself, which is not something that the Commission should gloss over, or ignore. When you think about it, the potential for the ATC to make a decision without understanding that relationship is a pretty, scary thought. That relationship should have been disclosed. But,

the Excise report shows more of a pattern of non-disclosures. The Excise officers point out the fail to disclose the relationship with primary sources of supply, by the question on the application. Those two are Shaw/Ross and Lauber Imports. They indicated there are no individuals—this is the next item—no individuals with an interest in the application held any other permit of any kind connected with the sale of alcoholic beverages. Southern replied, “not in Indiana”, which presents the problems which the Excise officers clearly laid out in their report, of requiring those to make full disclosures and allow a full investigation of those relationships need to be disclosed. The list of enforcement actions that Southern prided in response to the Excise officer’s queries also inaccurate. They list a TTV (?) investigation in Illinois as pending. What Southern didn’t disclose and what the Excise officers diligently uncovered is that Southern, as part of an offer of compromise, paid \$225,000 to TTV and Shaw/Ross paid an additional \$10,000 to settle those charges. Southern Indiana failed to reveal how it plans to service thousands of Indiana retailers around the State from a 3,500 square foot warehouse in the southern part of the State. Consistently tell this Commission that a joint venture is subject to regulatory approval without saying where, by whom, when, what the status of that is. And, finally, the Excise officers discovered a complaint in Nevada from a competitor of

(inaudible) clearing of all practice of creating written reports for goods that are not stored at a warehouse, basically a phony paper trail. That's the natural segway to the character issues, the pattern of anticompetitive conduct, which we brought to the Commission's attention with some civil lawsuits and the Excise officers found additional evidence of some very serious charges, both in New York and Illinois. The New York situation, Southern America was one of eight New York wholesalers who were fined a total of 1.6 million dollars for illegal marketing practices. They found that the problems there, getting involved, giving discounts to favored retailers, along with gifts, such as annex gift cards, free trips, iPods, golf clubs and gas grills. Southern and its affiliates paid a \$300,000 fine, not an insignificant sum even for Southern. The information in the report discloses that the scheme even involved sham credits to favored retailers in order to hide. So, now, they have misconduct, the covering up of the illegal conduct that is going on. The impact of that is pretty substantial of that. The New York investigators estimated the favored benefits to retailers exceeded 50 million dollars from 2003 -2005. Ran a lot of local business—the association estimated 1,000 liquor stores were put out of business and the New York authority had to devote 19 agents for several months to an investigation. You might think that Southern would have, that there might be a lesson learned from that situation, buy

yet, just a few years later there found a TTV investigated Southern for the very same type of conduct with a retailer in Illinois. So, it's not a situation where lessons were learned. These are not isolated incidents. The state liquor laws are really designed to be self-enforcing and as regulators, you need to be able to rely on wholesalers that will police themselves and that's not happening we would suggest at Southern. They pay a fine in New York and then they go on as they did in Illinois. We touched briefly on the regional distribution of wine and liquor. We know that that facility in southern Indiana is not large enough. Harvey Chaplin says in his interview, "We're looking at regional distribution centers, so our inventory doesn't get out of whack, because having every state buy inventory on its own increases your loans and costs of doing business." As the Excise officers have found, Southern has large warehouses just over the border in Chicago and Louisville and with the joint venture in place, you could have Olinger also being supplied from out-of-state. Contributing to that problem, there are differences in taxation systems in Illinois and Kentucky...Am I up?

Chairman

You're close. That's all right. I'll be fair to the other side as well, but...

Badger

Finally, I just want to touch briefly on the Commerce Clause argument, because again, it's just a distraction and a hollow threat. None of these reasonings that the permit,

grounds to deny the permit, have anything to do with Southern's ownership of having out-of-state owners and there's not a single case, Commerce Clause case, that's been cited, not a single case that we're aware of. It doesn't follow from the theory that denies a commission the ability to apply neutral, even-handed criteria, permitting criteria, and denying a permit on that basis. There is no Commerce Clause issue on any of this. We submit it's just a distraction. Spent so much time arguing that and completely ignored serious problems with the joint venture. It's frankly just an evasion. Bottom line, if the permits are approved, you'll have an unprecedented level of control of the Indiana market, all in the hands of this management team of the joint venture, which they've announced. That is not in the best interest of the Indiana consumer. It will harm the Indiana consumer.

Chairman

Thank you very kindly. I will allow you a moment or two to clean off the desk there and we'll have the other comments momentarily. That was about 23 minutes worth. I'm not requiring 23 minutes, but you sure are entitled to it, sir. Identify yourself, Mr. Badger, for the record.

Badger

I'm sorry. I'm Steve Badger. I'm with the law firm of Bose, McKinney and Evans. I'm representing National Wine & Spirits.

Chairman

That is my bad, not yours. Sir, identify yourself for the record.

Byron Leet                      Thank you. Byron Leet, l-e-e-t. I'm with the law firm of Wyatt Tarrant and Combs, here representing Southern Wine & Spirits.

Chairman                      Thank you. Make yourself at home.

Leet                              Let me say first of all that I appreciate your gracious offer to give me 23 minutes. I'm going to decline to use it, but I appreciate the offer. At this point, on behalf of Southern, basically just want to thank this Commission for the time and effort that has gone into review of these permit applications. It is no secret among anyone in this room that this has been a matter that has gained a lot of attention. Coincidentally, it turns out as I was reviewing the file, I see that it was a year ago, it will be a year tomorrow, that Southern initially was advised that the wine permit would be granted and the liquor permit would be denied. So, over the course of nearly one year, we know that a lot of time and energy has gone into this. On behalf of Southern, we genuinely appreciate it and we appreciate the Commission's efforts. I'm not going to try to respond to all the things that have been left out here. The sky is not falling. Southern is a very, reputable company, which distributes spirits and wine in some 29 states in the United States of America. It enjoys a very good reputation. We believe that both these permits should be granted and we would respectfully ask the Commission to grant them. But in any event, we appreciate

the Commission's time on this and the Commission's effort.

Thank you very much on behalf of Southern.

Chairman

Thank you very kindly. Is there any public comment besides the, for the lack of a better word, adversaries? Yes, sir.

John Livengood

Yes, sir, there is. My name is John Livengood. I'm president of the Association of Beverage Retailers, which is the package store industry you've heard referenced a couple of times here in previous testimony. I just want to start by saying that we work closely with both of the wholesalers in Indiana, major wholesalers, and I would be here today expressing the same concerns if it was the other way around, if it was Olinger objecting to the joint venture. Our concern, s retailers, is that the applications are a threat to competition, and if the permits are granted, the Indiana market would potentially be subject to the control of two, very, large wholesalers who have an alliance or a joint venture. The harms are likely to result in a monopoly that you've heard referenced. The answer in terms of a remedy for retailers is that there's none. The local retailer would have no place to turn. Second issue that we're concerned about is price discrimination. As national deals and discounts are cut in other states, on a national basis, it would be exceedingly difficult, if not impossible, for the ATC to regulate. There's always a concern at our level about what is going on at the national chain level. We're probably

going to discuss that this afternoon at a legislative hearing over at the Statehouse, as we discuss some other issues. But, in general, our interest, concern about the joint venture being allied with national accounts and national brands, the losers will be local retailers and, of course, consumers who have fewer alternatives, higher prices, and lower levels of service. So, we just wanted to make the Commission aware of our concerns. Thank you, very much.

Chairman I will allow rebuttal of that, if you wish. But, first, I need to know if there's any other public...to the extent that you want to rebut that, you may, sir.

Leet No.

Chairman Thank you. Just want to be fair. Anything else for the good of the order? Okay. That will then close the public debate on that. Are there motions to be made regarding pending apps?

Comm. Guthrie Mr. Chairman, we have in our possession, a Letter of Advice from the Attorney General of Indiana that advises us that the residency requirements contained in our statutes are unconstitutional and are a violation of the Commerce Clause. Based on that opinion, which I would like to be put in the minutes of this meeting, I would move we decline to apply the residency requirement mandated by Indiana Code 7.1-3-21-5, in this situation.

Vice Chair Johnson Second.

Chairman Discussion? Those in favor signify by saying, aye.

Guthrie	Aye.
Johnson	Aye.
Comm. Sturtz	Aye.
Chairman	Those opposed? Motion carries unanimously. Further business?
Sturtz	<p>Mr. Chairman, with your permission, I am prepared at this time to make motions concerning these two pending applications for permits. Before making the motions, I wish to state that the Commission members have given serious consideration to many factors and issues which would include, but not be limited to, the following: Indiana laws that charge the Commission with the responsibility to protect the economic welfare, health, peace and morals of the people of this state and the authority to regulate and limit the manufacture, sale, possession and use of alcoholic beverages; and the applicant, Southern of Indiana is a subsidiary of Southern of America, the nation's largest wholesaler. Southern of America (through subsidiaries) has recently settled trade practice violations in Illinois and New York; and litigation opinions involving other subsidiaries of Southern of America reveal that courts have found evidence of southern of America "raiding" employees from its competition following unsuccessful buy-out negotiations; and the business relationships of the applicant, including the vague and unexplained joint venture with an entity which has an interest in an Indiana wholesaler permit, which</p>

would tend toward adversely influencing the Indiana market; and the applicant's failure to voluntarily disclose business interests that would prevent the Commission from properly monitoring the future operations of an active permit; and the applicant's failure to fully explain to the Commission its future intentions about providing services to Indiana retailers. The commission is attempting to act in the best interest of Indiana consumers; therefore, I move that both the liquor and wine permit applications be denied.

Guthrie

Second.

Chairman

Discussion? Those in favor signify by saying, aye.

Johnson

Aye.

Guthrie

Aye.

Sturtz

Aye.

Chairman

Those opposed? Motion carries unanimously.